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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM 1951

No. 196

KIMBELL-DIAMOND MILLING COMPANY,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

PETITIONER'S REPLY TO BRIEF FOR THE RESPONDENT IN OPPOSITION

Introduction

We respectfully submit to the Court the following reply to the brief for the respondent in opposition to the granting of certiorari herein.

Reply Argument

I.

Admittedly, since different tax years are involved, the decision of the Tax Court in the earlier *Kimbell-Diamond Milling Company case* can act as an estoppel in the present proceeding "only as to those matters in the second proceeding which were actually presented and determined in the first suit." *Commissioner* v. *Sunnen*, 333 U.S. 591, 598.

In the brief filed by respondent in opposition to the granting of certiorari herein, respondent concedes that the judgment of the Tax Court in the earlier case of *Kimbell-Diamond Milling Company* v. *Commissioner*, 10 T.C. 7, approved a tax liability calculated by using the identical basis for which petitioner now contends. Respondent asserts, however, (Br., page 10) that the fact that the judgment was so framed does not work a collateral estoppel, and cites *Hartford-Empire Company* v. *Commissioner*, 137 F. (2d) 540 (C.A. 2), certiorari denied, 320 U.S. 787, as supporting this contention.

In so contending, and in representing to this Court that his position in the matter is supported by the authority cited, respondent neglected to inform the Court regarding fundamental differences that existed between the underlying situation present in the case at Bar, and that before the Court of Appeals for the

Second Circuit in *Hartford-Empire Company* v. *Commissioner, supra.*

In the earlier *Kimbell-Diamond Milling Company case,* the proceeding before the Tax Court was litigated to the very end. The judgment of the Tax Court was its own judgment, independently arrived at, and entered solely upon the basis of the pleadings, and the evidence adduced at the trial. As we have shown in our opening brief, (Br. pp. 21-31) it was a *determination by that Court* of all of the issues involved in the case then before it, including the basis issue.

In *Hartford-Empire Company* v. *Commissioner, supra,* the situation was directly to the contrary. In the earlier *Hartford-Empire Company case,* the parties stipulated the "cost" of certain patents. The issues submitted for the decision of the Court by the pleadings and briefs of the parties in the first proceeding were confined to two questions, viz.: (1) Whether the taxpayer there was entitled to any allowance at all for the exhaustion of its patents; and (2) whether the taxpayer should be allowed to carry over the earlier year loss of a predecessor corporation.

In deciding the estoppel issue raised in the second *Hartford-Empire Company case,* the Court (137 F. (2d) 540, 541) said:

> "The first question is whether this decision (the earlier Tax Court judgment entered pursuant to a stipulation between the parties litigant) required

the Commissioner to use the same 'basis' for depreciation for the years now in question. That the Tax Court's former orders were a conclusive bar for the years 1923 to 1928 nobody disputes; but each year's tax is a separate 'cause of action' in the sense that that phrase is used for purposes of estoppel, and the estoppel depends upon whether the actual point was decided and was necessary to the decision. It is true that the Tax Court's actual orders assessing the deficiency—the final judgments—could not have been entered as they were unless the 'basis' for depreciation of the Empire and Howard patents had been taken at their cost to the taxpayer; but *actually the Court could not decide that question at all, for the stipulation did not present to it any other 'basis' for depreciation of the patents.* If the orders created any estoppel, it was therefore because the Commissioner had conceded the point and judgment had been entered upon his concession. *Had the issue—though it was an issue of law—been actually litigated and decided, we may assume arguendo that the Commissioner would have been estopped. Tait* v. *Western Maryland Railway Co.*, 289 U.S. 620, 53 S.Ct. 660, 77 L. Ed. 1470. Indeed, we may also assume that, since the petitions alleged and the Commissioner denied that the 'cost' to the taxpayer had been in the amounts stated and since the parties had agreed to the amounts, any future dispute about the amount was precluded, if that ever became relevant to a later contest between the parties. Restatement of Judgments, Sec. 68; Comment f, top of p. 304." (Matter in parentheses and emphasis supplied.)

We respectfully submit that *Hartford-Empire Company* v. *Commissioner*, *supra*, cited and relied upon

by respondent as controlling the disposition of the estoppel issue present in the instant proceeding, far from furnishing grounds for the denial of certiorari in the case at Bar, advances cogent reasoning why the petition herein for certiorari should be granted.

II.

The decisions below, and respondent's brief in opposition to the granting of certiorari herein, both confuse *purpose*, and ultimate *result*, with the "substance" of what was done, differences this Court, in the past, has had no difficulty in recognizing and giving effect to.

It should first be observed that, in the case at Bar, we are not concerned with a statutory "re-organization," and the doctrine that, in such cases, a particular act may be denied independent tax significance if the trier of facts finds that it was merely one of several interconnected steps in an over-all plant of reorganization (Cf: *Minnesota Tea Company* v. *Helvering*, 302 U.S. 609) has no application.

Concededly, in tax matters, as in other litigation, it is proper, where material, to look through "form" and be guided by "substance." Thus an instrument that in form is an absolute conveyance, but is intended by the parties to be, and is, a mere security device, will be recognized as such. *Helvering* v. *F. & R. Lazarus & Co.*, 308 U.S. 252. And where a corporation has made an effective sale of assets, and then proceeds to

dress the transaction in the guise of a purported liquidation followed by a stockholders sale, effect will be given to what was actually done. *Commissioner* v. *Court Holding Company*, 324 U.S. 331.

This does not mean, however, that, where there are two permissible methods of reaching a given end result, each of which methods has differing tax consequences, what is actually done can be ignored, and the transaction treated as being in "substance" something other than what it actually was. *United States* v. *Cumberland Public Service Company*, 338 U.S. 451; *Appeal of Minnie C. Brackett, Administratrix*, 19 B.T.A. 1154.

In the case at Bar, the taxpayer did exactly what it purported to do. It bought the entire capital stock of Whaley Mill and Elevator Company and thereafter dissolved that corporation. The legal effect of what was thus actually done is governed by the controlling provisions of express and unambiguous statutes. Such legal effect may not be changed or varied by saying that the "substance" of the transaction was something other than it actually was, merely because the same end result might have been reached in another way, to-wit, by a direct purchase of assets. *United States* v. *Cumberland Public Service Company, supra.*

The parties having stipulated (R. 55) and the Tax Court having twice found (10 T.C. 7, page 9, and R. 127) that petitioner acquired the entire capital stock of Whaley Mill and Elevator Company, and thereafter liquidated that corporation, under the plain language

of Sections 112(b)(6) and 113(a)(15) of the Internal Revenue Code, petitioner is clearly entitled to Whaley's basis for the assets acquired by it in connection with the complete liquidation of Whaley.

Conclusion

For the foregoing reasons, and for the reasons set out in the petition and the brief in support thereof, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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